

STATE OF NORTH DAKOTA
OFFICE OF SECURITIES COMMISSIONER

IN THE MATTER OF:)
)
Preferred Trust and Management,)
LTD, Gerald Henry, Dennis Skarphol,)
and Brian Henry - Consolidated Hearing)
)
Respondents.)
.....

**RECOMMENDED
FINDINGS OF FACT,
CONCLUSIONS OF LAW,
AND ORDER**

On April 10, 2001, the Securities Commissioner issued a separate Cease and Desist Order, Notice of Civil Penalty, and Notice of Right to Request a Hearing to each of the three above named individuals. On June 28, 2001, the Commissioner issued a separate Notice of Intent to Seek Civil Penalties to each of the three above named individuals. On June 22, 2001, the Securities Commissioner requested the designation of an administrative law judge ("ALJ") from the Office of Administrative Hearings to conduct a hearing and to issue recommended findings of fact and conclusions of law, and a recommended order in regard to each of these three matters. On June 25, 2001, the undersigned ALJ was designated to preside as hearing officer.

The ALJ consolidated these three separate matters because the same attorney, Mr. Michael R. Hoffman of Bismarck, represented all three individuals and the three matters were similar. Both parties agreed to consolidation.

On July 11, 2001, the Respondents filed a Motion and Brief to Dismiss this matter. On July 19, 2001, the Commissioner filed a brief in opposition. On July 20, 2001, the ALJ filed his Recommended Order Denying Motion to Dismiss. On July 31, 2001, the Commissioner filed

her Order Denying Motion to Dismiss. A prehearing conference on these matters was scheduled for September 7, 2001, but not held. However, telephone conferences were held involving the ALJ and counsel for the parties.

The Respondents appealed the Commissioner's July 31 Order to the District Court and eventually to the Supreme Court. Respondents also moved to stay the administrative proceeding until a decision by the courts. On September 6, 2001, the ALJ issued an Indefinite Postponement of this matter. On April 15, 2003, the Supreme Court issued its decision. *Henry, et al v. Commissioner*, 2003 ND 62. The Court dismissed the appeal because it said the Commissioner's July 31, 2001, Order was not a final order.

On May 8, 2003, the ALJ issued a Notice of Consolidated Hearing. The hearing was held as scheduled on June 6, 2003, in the Office of Administrative Hearings, Bismarck, North Dakota. Special Assistant Attorney General Matthew O. Bahrenburg represented the Securities Commissioner. The Respondents were all present and were represented at the hearing by Mr. Hoffman. The Securities Commissioner called one witness, its investigator and examiner, Kelley Mathias. During the course of his testimony Mr. Mathias was qualified as and declared an expert on high yield investment fraud and prime bank fraud. The Commissioner offered 23 exhibits (A-W), exhibit D was withdrawn. The rest of the exhibits were all admitted, most, if not all, over objection. All of the individual respondents refused to testify, pleading their 5th Amendment right to refuse to testify against themselves.

On June 17, 2003, the Commissioner filed a "Post-Hearing Brief and Closing Argument." On June 30, 2003, the Respondents filed their "Concluding Argument of Each Respondent." On July 2, 2003, the ALJ received the Commissioner's correspondence stating that no reply brief would be filed. Accordingly, the record in this matter was closed on July 2, 2003, pending the

issuance of the hearing officer's recommended decision and the final decision of the Securities Commissioner.

Based on the evidence presented at the hearing and the briefs of the parties, the administrative law judge makes the following recommended findings of fact and conclusions of law.

FINDINGS OF FACT

1. The Securities Commissioner investigated the activities of Mr. Frederick W. Keiser of Minot and seized a computer from him. As a result of that investigation, separate Cease and Desist orders were issued against Preferred Trust & Management, LTD. ("Preferred Trust") and, amongst others, the three individual respondents in this matter.

2. Much of the documentary evidence offered and admitted at the hearing in this matter was documentary evidence obtained from Mr. Keiser's computer or from the website of Preferred Trust. The entire contents of the Keiser computer and hard drive, according to the assertions of Mr. Bahrenburg, voluminous contents, were transferred to exhibit D, a CD. All of the exhibits offered by the Commissioner, except exhibits S, T, & U (transcripts of testimony of three witnesses in a civil proceeding regarding Preferred Trust and Mr. Keiser), and exhibits A, B, and C were taken from exhibit D and copied in hard form. Exhibits A, B, and C are documents copied from the website of Preferred Trust.

3. Exhibits A-C, as well as exhibits E-W, identify Preferred Trust as a fraudulent investment scheme. Mr. Mathias testified that Preferred Trust was a fraudulent investment scheme. There was no evidence offered to the contrary.

4. The Preferred Trust investment scheme (hereinafter the "scheme") is a security as defined in N.D.C.C. 10-04-02(15).

5. The scheme was not registered as a security in North Dakota and is not exempt from registration under the Securities Act. N.D.C.C. §§ 10-04-04; 10-04-05. Neither is the scheme an exempt transaction under N.D.C.C. § 10-04-06.

6. The respondent, Gerald Henry, is not currently and has never been registered as a securities investment advisor representative or securities agent in North Dakota.

7. The respondent, Dennis Skarphol, is not currently and has never been registered as a securities investment advisor representative or securities agent in North Dakota.

8. The respondent, Brian Henry, is not currently and has never been registered as a securities investment advisor representative in North Dakota. Brian Henry has been registered as a securities agent in North Dakota. His registration as a securities agent was approved August 24, 2000. However, exhibits J and K, documents copied from the Keiser computer, show entries regarding a Brian Henry in a March 31, 2000, monthly statement and an April 30, 2000, monthly statement.

9. The evidence shows, by the greater weight of the evidence, that the three respondents are the same individuals as those three individual named and listed in various places in the exhibits admitted at the hearing. The addresses for two of the individuals named in the exhibits are same as the addresses at which the respondents accepted service of the pleadings in this matter (Gerald Henry and Dennis Skarphol). In regard to the respondent Brian Henry, a record search shows a Brian Henry, a North Dakota resident, living at the same address as Gerald Henry. From all of the evidence, it may be inferred that the Brian Henry named and listed in various places in the exhibits is the same Brian Henry registered with the Securities Commissioner in 2000 and the same Brian Henry who is a respondent in this matter.

10. The documents admitted at the hearing show that on the Keiser computer each of the respondents is listed as having referred other individuals to the scheme (Gerald Henry referred eight individuals; Dennis Skarphol referred four individuals; and Brian Henry referred one individual). However, there is no evidence showing an offer or sale of any security by any of these three respondents. There is no evidence showing any transaction between any of the respondents and someone underneath them or someone somehow related in a business or other fashion to them in the scheme's records in evidence, *i.e.*, there is no evidence of a purchase. There is no record of any payment being made by anyone for anything. The evidence only shows that the three respondents were entitled to compensation from securities referrals, and monies were possibly earmarked for them, but no actual offer or sale has been proven. The exhibits show nothing conclusive, only possibilities based on an inadequate amount of information.

11. There is no evidence showing that the words "referred" or "entitled to receive" or "earmarked," frequently used in documents or testimony at the hearing to apply to activities of the three respondents, equate with the statutory requirements of the words "offer," "sale," and "purchase."

12. Similarly, as the evidence does not show any offer, sale, or purchase of any security, directly or indirectly, only the possibility of offer, sale, or purchase of securities, it also does not show any "device, scheme, or artifice to defraud" investors employed by any of the respondents in any offer, sale, or purchase of securities. N.D.C.C. § 10-04-15. Clearly, the scheme is a "device, scheme, or artifice to defraud." But, any evidence, especially anything direct, proving a conclusive connection between the respondents and anyone else is missing. Possibilities are certainly evident, but, again, the evidence conclusively showing it is missing.

COMMENTARY ON FINDINGS OF FACT

Without the testimony of one or more of the respondents in this administrative matter, possibly testimony from one of the respondents in the other, related administrative matters, evidence from Mr. Keiser, or evidence from one or more of the individuals "referred" by one or more of the respondents in this matter, or some other evidence, documentary or otherwise, that connects these respondents in an offer, sale, and purchase, the Securities Commissioner's case is not proven by the greater weight of the evidence. Based strictly on the documentary evidence, which is really all the evidence there is in this matter, except for Mr. Matthias's opinions, there are too many possibilities for what actually could have occurred to draw any conclusive determinations regarding the respondents and what actually did occur with regard to violations of the securities law. Adverse inferences can, perhaps, be drawn from a failure to testify. But, the inferences in this matter cannot substitute, for real, credible evidence. What should the inference be? There is simply not enough probative evidence from which to draw an adverse inferences that the Respondents violated the law as alleged. Such inferences would border on speculation.

Certainly, other individuals have settled other similar matters regarding the Preferred Trust investment scheme with the Securities Commissioner, with penalties imposed against the respondents in those proceedings as a result of settlement. This too is telling. But, a violation by others does not necessarily mean violations by the Respondents. Again, there is no evidence in this matter conclusive enough to do more than state there is a good possibility that the respondents in this matter were engaged in actions in violation of the law as alleged in the Cease and Desist Order. However, there are other possibilities, too. The Commissioner's burden of proof in this matter simply is not met. Even with a knowledge that others were in violation in

similar circumstances, based on the evidence presented at this hearing, the leap in logic that the hearing officer is asked to make is too great.

In regard to the cases cited in the Commissioner's brief, the ALJ believes that they can be distinguished. They do not apply to this matter, at least to the extent that the Commissioner would have them apply. *Baxter* involved an inmate disciplinary hearing and the inmate's failure to testify at those proceedings. He was charged with inciting and creating a disturbance while in prison. He was notified from the outset that his silence may be used against him. The Court allowed an inference to be drawn against him for failure to testify. 425 U.S. 308, 318 (1976). *Bilokumsky* involved a deportation proceeding in which the government sought to deport Bilokumsky for being an alien and advocating the overthrow of the government. Bilokumsky had admitted upon his arrest that he was an alien. At the proceeding he did not testify. He subsequently claimed that the government did not prove its case that he was an alien. At the hearing the government only offered certain documents advocating the overthrow of the government that had been found in Bilokumsky's possession. It inferred from his silence that he was an alien. In regard to the question of him being an alien, the Court said that Bilokumsky had a strong reason for claiming citizenship if he was one and his failure to do so could be used against him to prove he was an alien. There could have been no harm to Bilokumsky claiming he was a citizen, if he was one. 263 U.S. 149, 153-154 (1923). In *Beers*, a civil action on trespass in a car accident, evidence was presented by the plaintiffs; the defendants did not testify about the accident and, their failure to testify was held against them. There was no 5th Amendment claim. 151 A.2d 465 (1959). In *Dommes* there were witnesses who described the action in question in some detail and there had been a statement made to the police by a party.

Thus, that party's failure to testify could be used to support an inference that whatever evidence he would have given would have been unfavorable. 38 A.2d. 73, 75 (1944).

The inferences the Commissioner asks to be drawn in this matter, cannot be drawn based on the facts and circumstances of this matter.

CONCLUSIONS OF LAW

The greater weight of the evidence does not show any violations of N.D.C.C. ch. 10-04 by Brian Henry, Gerald Henry, or Dennis Skarphol.

RECOMMENDED ORDER

Because the greater weight of the evidence shows that neither Brian Henry, nor Gerald Henry, nor Dennis Skarphol violated any of the provisions of N.D.C.C. ch. 10-04, the Cease and Desist Order issued against each of them is **dismissed**.

Dated at Bismarck, North Dakota, this 23rd day of July, 2003.

State of North Dakota
Karen Tyler
Securities Commissioner

By: _____
Allen C. Hoberg
Administrative Law Judge
Office of Administrative Hearings
1707 North 9th Street
Bismarck, North Dakota 58501-1882
Telephone: (701) 328-3260